

Message Text

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PAGE 01 OTTAWA 01064 01 OF 03 021714Z
ACTION EB-08

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INFO AMCONSUL MONTREAL
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LIMITED OFFICIAL USE SECTION 01 OF 03 OTTAWA 01064

DEPT. PASS CEA, TREAS, FRB

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TAGS: ECON, EFIN, CA
SUBJECT: RECENT ECONOMIC AND FINANCIAL DEVELOPMENTS.

1. SUMMARY. IN SPEECH BEFORE LIBERAL PARTY CONVENTION, PM TRUDEAU REITERATED THEME STRESSED AT FEDERAL/PROVINCIAL ECONOMIC SUMMIT THAT CANADA IS A HEALTHY ECONOMY IN TOUGH, COMPETITIVE WORLD. FINANCE MINISTER CHRETEN IN TELEVISED STATEMENT GAVE DETAILED DEFENSE OF GOC ECONOMIC POLICIES. HOWE RESEARCH INSTITUTE CALLED FOR TAX CUTS TO AVERT RISE IN UNEMPLOYMENT RATE IN 1978. GOC PROJECTS 9.8 PERCENT RISE IN FEDERAL GOVERNMENT SPENDING IN FY 1978/79 (SEPTTEL). NEW ORDERS RISE, UNFILLED ORDERS OFF. STATCAN SURVEY POINTS TO FALL IN REAL PRIVATE INVESTMENT SPENDING IN 1978. TOURISM DEFICIT REACHED CDOLS 1.66 BILLION IN 1977, UP CDOLS 464 MILLION FROM 1976 LEVEL. TRADE SURPLUS NARROWED IN JANUARY. FIRA CRITICIZED RE CONTROL OF FOREIGN DIRECT INVESTMENT INFLOWS. CAPITAL AND EXCHANGE MARKETS SETTLED DOWN IN WEEK ENDING FEBRUARY 24 ON NEWS OF GOC'S BOLSTERING
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PAGE 02 OTTAWA 01064 01 OF 03 021714Z

OF DOLLAR'S DEFENSE. CHRETEN ANNOUNCED ON FEBRUARY 28 THAT GOC WOULD DRAW DOWN U.S.DOLS 1.5 BILLION STANDBY CREDIT BY U.S.DOLS 200 MILLION. END SUMMARY.

2. DOMESTIC DEVELOPMENTS. AWARE THAT POLITICAL OPPOSITION PLANS TO MAKE STATE OF THE ECONOMY CENTRAL ISSUE IN FORTH-COMING FEDERAL ELECTIONS (AS YET UNSCHEDULED), PM TRUDEAU

CONTINUED THEME AT FEBRUARY 24 LIBERAL PARTY CONVENTION (SEE OTTAWA 987) THAT CANADA IS NOT A SICK ECONOMY IN A HEALTHY WORLD BUT A HEALTHY ECONOMY IN A TOUGH, INCREASINGLY COMPETITIVE ENVIRONMENT. FINANCE MINISTER CHRETEN PICKED UP THEME IN FEBRUARY 26 TELEVISED SPEECH GIVING DETAILED DEFENSE OF GOC ECONOMIC POLICIES. CHRETEN EMPHASIZED THAT CANADIAN ECONOMY HAS PERFORMED WELL RELATIVE TO THOSE OF OTHER INDUSTRIALIZED COUNTRIES AND REITERATED VIEW THAT ECONOMY WOULD GROW BY 5 PERCENT IN 1978.

3. HOWE RESEARCH INSTITUTE (HRI) TOOK LESS SANGUINE VIEW OF SHORT RUN PROSPECTS IN ITS ANNUAL POLICY REVIEW. HRI INDICATED THAT PERMANENT CUT IN TAXES (PREFERABLY IN SALES TAXES) WOULD BE NECESSARY TO ACHIEVE REAL GNP GROWTH AT A RATE SUFFICIENT TO KEEP UNEMPLOYMENT RATE FROM RISING THIS YEAR. HRI UNDERLINED NEED FOR STRUCTURAL ADAPTION, REGIONAL DIFFERENTIATION OF FISCAL POLICIES AND LESS GOVERNMENT REGULATION. HRI ALSO FOCUSED ON NEED FOR INTENSIFIED PUBLIC DEBATE AND ANALYSIS OF ECONOMIC ISSUES, WITH MAJOR ROLE PLAYED BY ECONOMIC COUNCIL OF CANADA.

4. OUTLOOK FOR INVESTMENT SPENDING CONTINUES WEAK. STATCAN SEMI-ANNUAL INVESTMENT SURVEY PUTS INTENDED PUBLIC AND PRIVATE INVESTMENT SPENDING AT CDOLS 48.9 BILLION IN 1978, UP 4.8 PERCENT FROM 1977 LEVEL. SINCE SURVEY INDICATES THAT CAPITAL GOODS PRICES COULD RISE BY ABOUT 7 PERCENT, LIMITED OFFICIAL USE

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PAGE 03 OTTAWA 01064 01 OF 03 021714Z

4.8 PERCENT NOMINAL INCREASE REPRESENTS REAL DECLINE OF ABOUT 2 PERCENT. IN NOMINAL TERMS, PUBLIC INVESTMENT TO RISE BY 4 PERCENT AND PRIVATE INVESTMENT BY 3.4 PERCENT. INVESTMENT BY UTILITIES EXHIBITS STRONGEST RISE (13.7 PERCENT), WHILE INVESTMENT IN MINING, QUARRIES AND OIL WELLS SHOWS MOST SEVERE DECLINE (6 PERCENT). ONLY UTILITIES AND COMMERCIAL SERVICES SHOW INCREASE IN REAL INVESTMENT IN 1978.

5. COMMENT. RESULTS OF STATCAN SEMI-ANNUAL SURVEY ARE GENERALLY CONSISTENT WITH THOSE OF INDUSTRY, TRADE AND COMMERCE (IT&C) INVESTMENT SURVEY WHICH CONCLUDED THAT REAL INVESTMENT SPENDING COULD FALL BY ABOUT 1.6 PERCENT THIS YEAR. (OTTAWA 9909, 1977). BOTH SURVEYS SEE CONSIDERABLE STRENGTH IN UTILITIES INVESTMENT AND DECLINE IN ENERGY AND MANUFACTURING INVESTMENT. IN ADDITION, BOTH SURVEYS CONCLUDE THAT INVESTMENT SPENDING WILL BE WEAKER IN 1978 THAN IT WAS LAST YEAR. SUBSTANTIAL EXCESS PRODUCTIVE CAPACITY AND ECONOMIC/POLITICAL UNCERTAINTY CONTINUE AS MAJOR FACTORS DEPRESSING PRIVATE (NON-ENERGY) INVESTMENT. DEGREE OF DOWNSIDE RISK ATTACHED TO EMBASSY'S PROJECTION OF 1.5 - 2.0 PERCENT RISE IN REAL INVESTMENT

SPENDING THIS YEAR HAS CLEARLY INCREASED. END COMMENT.

6. SEASONALLY ADJUSTED VALUE OF SHIPMENTS IN MANUFACTURING REACHED CDOLS 9.6 BILLION IN DECEMBER, UP 4.3 PERCENT FROM NOVEMBER AND 14 PERCENT ABOVE LEVEL OF DECEMBER, 1976. NEW ORDERS STOOD AT CDOLS 9.7 BILLION IN DECEMBER, AN INCREASE OF 2 PERCENT FROM NOVEMBER AND OF 5.5 PERCENT FROM DECEMBER 1976. UNFILLED ORDERS, HOWEVER, DECLINED SLIGHTLY BETWEEN NOVEMBER AND DECEMBER. RATIO OF TOTAL OWNED INVENTORIES TO SALES DROPPED FROM 2.0 IN NOVEMBER TO 1.91 IN DECEMBER.

7. GOVERNMENT SPENDING: GOC RECENTLY INTRODUCED INTO

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PAGE 01 OTTAWA 01064 02 OF 03 021722Z
ACTION EB-08

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LIMITED OFFICIAL USE SECTION 02 OF 03 OTTAWA 01064

PARLIAMENT OFFICIAL ESTIMATES FOR FEDERAL GOVERNMENT SPENDING FY 1978/79. ESTIMATES CONSISTENT WITH GOC VIEW THAT REAL GOVERNMENT SPENDING SHOULD RISE LESS RAPIDLY THAN GROWTH OF POTENTIAL OUTPUT. OFFICIAL PROJECTIONS SHOW NOMINAL SPENDING RISE OF 9.8 PERCENT IN FY 1978/79 AND REAL INCREASE OF 3.5 PERCENT (SEE SEPTTEL).

8. EXTERNAL DEVELOPMENTS. TOURISM DEFICIT. TRAVEL DEFICIT REACHED CDOLS 1.7 BILLION IN 1977, COMPARED WITH CDOLS 1.2 BILLION DEFICIT REGISTERED IN 1976. VOLUME OF CANADIAN TRAVEL TO U.S. AND TO OTHER COUNTRIES ROSE BY 5.5 PERCENT AND 12.3 PERCENT RESPECTIVELY, WHILE VOLUME OF U.S. AND OTHER FOREIGN TRAVEL IN CANADA DECLINED BY 1.4 PERCENT AND 9.7 PERCENT. TOTAL CANADIAN EXPENDITURES ABROAD ROSE BY

17.3 PERCENT WHILE FOREIGN EXPENDITURES IN CANADA INCREASED BY 3.9 PERCENT. ALTHOUGH TRAVEL DEFICIT WIDENED IN 1977 AS A WHOLE FROM 1976 LEVEL, FIGURES FOR NOVEMBER AND DECEMBER REFLECTED FAVORABLE IMPACT ON TRAVEL DEFICIT OF CANADIAN DOLLAR DEPRECIATION.

9. TRADE. SEASONALLY ADJUSTED JANUARY MERCHANDISE TRADE SURPLUS LIMITED OFFICIAL USE

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PAGE 02 OTTAWA 01064 02 OF 03 021722Z

WAS CDOLS 306 MILLION, COMPARED WITH DECEMBER SURPLUS OF CDOLS 435 MILLION. ON BALANCE OF PAYMENTS BASIS EXPORT VALUE FELL BY 16.9 TO CDOLS 3.5 BILLION, WHILE IMPORTS WERE OFF BY 15.5 PERCENT TO CDOLS 3.2 BILLION. BOTH EXPORT AND IMPORT VALUES DECLINED ON AVERAGE IN THREE MONTH PERIOD ENDING JANUARY FROM AVERAGE OF PREVIOUS THREE MONTHS. EXPORTS FELL BY 2.2 PERCENT, IMPORTS BY 3.3 PERCENT.

10. FOREIGN INVESTMENT. ARTICLE BY PHILIP TEASDALE IN FEBRUARY 25 FINANCIAL POST ALLEGED FIRA TOO LENIENT IN APPROVING FOREIGN DIRECT INVESTMENT APPLICATIONS. TEASDALE NOTED CRITICALLY THAT ACCORDING TO FIRA STATISTICS, APPLICATIONS TO START NEW BUSINESSES ROSE BY 74 PERCENT IN 1977, THAT TAKEOVER APPLICATIONS WERE UP BY 56 PERCENT, AND THAT FIRA'S APPROVAL RATE IS RUNNING AT 90 PERCENT. HE FINDS FIRA APPROVAL HIGH IN VIEW OF FACT THAT RECENT IT&C STUDY CONCLUDED THAT EXISTING LEVEL OF FOREIGN OWNERSHIP COULD BE "SIGNIFICANT IMPEDIMENT" TO IMPROVING CANADIAN MANUFACTURING PERFORMANCE. (COMMENT. IT&C STUDY OF MANUFACTURING SECTOR, PREPARED FOR FEDERAL/PROVINCIAL ECONOMIC SUMMIT, INDICATED THAT FOREIGN OWNERSHIP COULD HAVE SUCH AN EFFECT IF FIRMS WERE GEARED TO THE CANADIAN MARKET, BUT THAT IT COULD FACILITATE GREATER EFFICIENCY IF COMPANIES WERE PRODUCING FOR NORTH AMERICAN MARKET. OF COURSE, SAME STATEMENT COULD BE MADE OF FIRMS WHOLLY OWNED BY CANADIANS.) ARTICLE CITES FIRA COMMISSIONER HOWARTH AS STATING THAT HIGH APPROVAL RATE MAINLY REFLECTS IMPROVED FIRA EFFICIENCY AND BETTER COMMUNICATION WITH PROSPECTIVE INVESTORS RATHER THAN SHIFT TOWARD INCREASED LENIENCY.

11. CAPITAL MARKETS. CAPITAL MARKETS SETTLED DOWN IN WEEK ENDING FEBRUARY 24 AS DOWNWARD PRESSURE ON CANADIAN DOLLAR SUBSIDED. INTEREST RATE ON THREE MONTH TREASURY LIMITED OFFICIAL USE

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PAGE 03 OTTAWA 01064 02 OF 03 021722Z

BILLS WAS 7.30 COMPARED WITH 7.26 PREVIOUS WEEK. LONG TERM RATES WERE UP SLIGHTLY.

12. MONEY SUPPLY. BANK OF CANADA (BOC) HAS REVISED MONEY SUPPLY STATISTICS. PREVIOUSLY, ENTIRE AMOUNT OF ESTIMATED "FLOAT" HAD BEEN DEDUCTED FROM GROSS DEMAND DEPOSITS IN CALCULATING NET DEPOSITS AND HENCE IN ESTIMATING VARIOUS MONETARY AGGREGATES. HENCEFORTH, FLOAT RELATE TO TRANSACTIONS BETWEEN GOVERNMENT AND BOC WILL NOT BE DEDUCTED FROM GROSS DEPOSITS. BOC INDICATES THAT NEW PROCEDURE WILL GIVE MORE ACCURATE ESTIMATE OF NET LEVEL OF PRIVATELY HELD DEPOSITS. BOC NOTES DIFFERENCE IN PROCEDURES CAN ALTER CONSIDERABLY ESTIMATES OF WEEK TO WEEK CHANGES IN MONEY SUPPLY, BUT HAS LITTLE EFFECT ON LONGER TERM GROWTH TRENDS OF THE AGGREGATES. REVISED FIGURES BACK TO 1966 WILL BE PUBLISHED IN FEBRUARY BOC REVIEW.

13. ACCORDING TO REVISED STATISTICS (SEASONALLY ADJUSTED) M1 STOOD AT CDOLS 19.7 BILLION IN JUNE, 1977 (BASE FOR CALCULATING TARGET RANGE OF M1 GROWTH) AND AT CDOLS 20.7 BILLION IN JANUARY, 1978. THUS, BETWEEN JUNE AND JANUARY M1 GREW AT SEASONALLY ADJUSTED ANNUAL RATE OF 10.2 PERCENT. IN 12 MONTHS TO JANUARY, M1 GREW BY 11.3 PERCENT. M1B (M1 PLUS CHECKABLE SAVINGS DEPOSITS) ROSE AT ANNUAL RATE OF 9.6 PERCENT BETWEEN JUNE AND JANUARY AND BY 10.5 PERCENT IN 12 MONTHS TO JANUARY. SIMILAR CALCULATIONS FOR M2 SHOW GROWTH RATES OVER THESE PERIODS OF 10.5 PERCENT AND 10.9 PERCENT RESPECTIVELY.

14. EXCHANGE MARKETS. EXCHANGE MARKETS SETTLED DOWN IN WEEK ENDING FEBRUARY 24 WITH ANNOUNCEMENT THAT GOC WOULD

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PAGE 01 OTTAWA 01064 03 OF 03 021727Z
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LIMITED OFFICIAL USE SECTION 03 OF 03 OTTAWA 01064

DRAW DOWN U.S. DOLS 1.5 BILLION STANDBY CREDIT AND ARRANGE FOR ADDITIONAL INTERNATIONAL BORROWING TO BOLSTER DEFENSE OF DOLLAR. AVERAGE EXCHANGE RATE FOR WEEK WAS 89.57 U.S. COMPARED WITH 89.66 U.S. PREVIOUS WEEK.

15. ON FEBRUARY 24 CHRETIEN ANNOUNCED THAT GOC WILL MAKE A U.S. DOLS 200 MILLION DRAWDOWN ON STANDBY CREDIT. TERMS OF DRAWDOWN (SET LAST FALL WHEN STANDBY WAS NEGOTIATED) WILL INCLUDE INTEREST RATE OF 0.625 PERCENT ABOVE LONDON INTERBANK OFFER RATE (LIBOR). SINCE TRANSACTION WILL NOT BE COMPLETED BEFORE END OF FEBRUARY, IT WILL NOT EFFECT OFFICIAL RESERVE FIGURES FOR THE MONTH. ENDERS

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